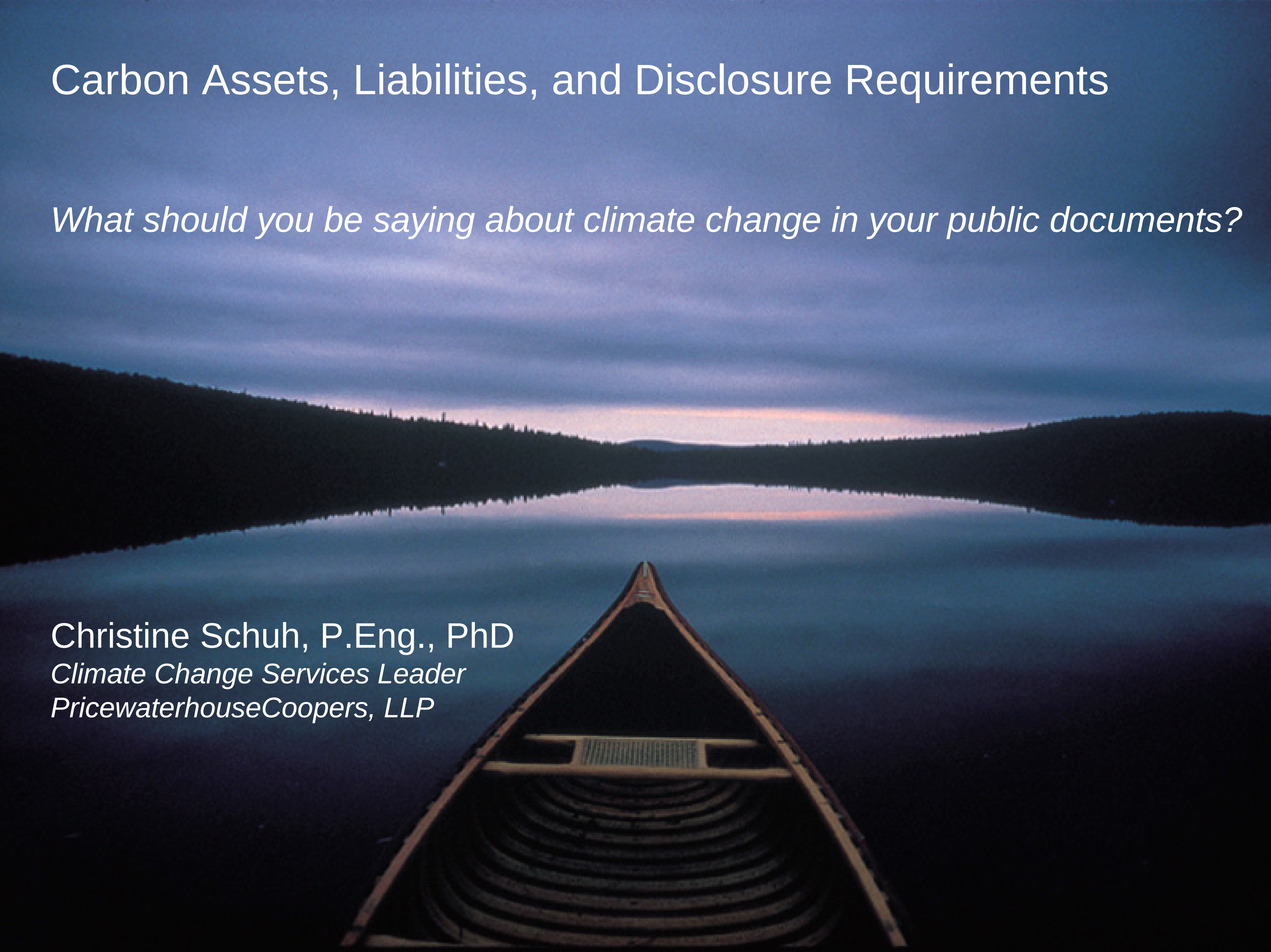

# Carbon Assets, Liabilities, and Disclosure Requirements

*What should you be saying about climate change in your public documents?*

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# Agenda

What is a carbon asset?

What is a carbon liability?

What carbon assets and liabilities must be disclosed?

How do you evaluate carbon assets and liabilities?

What is carbon risk?

What does carbon risk have to do with disclosure?

What is carbon risk management?

What should you be disclosing?

# What is a Carbon Asset?

Assets have three essential characteristics:

- Has the capability to contribute directly or indirectly to future net cash flows;
- The company can control the asset; and
- The transaction or event giving rise to the company's right to, or control of, the asset has already occurred.

# What is a Carbon Asset?

Carbon assets (intangible assets) include:

- offsets (carbon credits)
- facilities that generate performance credits
- allowances

Intangible assets are non-monetary assets that cannot be seen, touched or physically measured and which are created through time and/or effort.

# What is a Carbon Liability?

A liability is an ***obligation*** of a company arising from ***past*** transactions or events, the settlement of which may result in the transfer or use of assets, provision of services, or other yielding of economic benefits in the future.

- a duty or responsibility to others
- entails a settlement by future transfer or use of assets, provision of services or other yielding of economic benefits
- occurs at a specified or determinable date, on a specified event, or on demand
- little or no discretion to avoid it
- historical transaction

# What is a Carbon Liability?

Liabilities in financial accounting need not be legally enforceable; but can be based on equitable obligations or constructive obligations.

- an equitable obligation is a duty based on ethical or moral considerations.
- a constructive obligation can be inferred from a set of facts in a particular situation as opposed to a contractually based obligation.

# What is a Carbon Liability?

Carbon liabilities could include the difference between:

- actual emissions and regulatory emission limits,
- actual emissions and allowances,
- actual emissions and public statements made by senior officials about emission targets,
- actual performance and performance targets established by contracts with other parties (e.g., joint venture partners), and
- actual performance and societal expectations of emission reductions.

# What Carbon Assets and Liabilities Must be Disclosed?

What is material?  Would the information influence a reasonable investor in deciding whether to invest or continue to invest in a company?

# What Carbon Assets and Liabilities Must be Disclosed?

## Who is effected?

companies representing 40% of TSE’s total market capitalization would be directly affected by a legislated system of GHG emissions caps and trading (Wood-Gundy)

## What is the level of investor’s interest?

- *Shareholder resolutions*
- *Investor Network on Climate Risk*
- *Carbon Disclosure Project*
- *UNEP Finance Initiative*
- *WRI studies*
- *Mercer Investment Consulting*
- *NRTEE Capital Markets report*

- *US Climate Action Partnership*
- *CCCE Environmental Leadership Task Force*
- *Investor Statement on Climate Change*
- *Global Framework for Climate Risk Disclosure*

# What Carbon Assets and Liabilities Must be Disclosed?

There is no clear cut answer because it depends on your business.

What is considered ***material*** is changing.

Factors to consider:

| | |
|---|---|
| • carbon footprint | (exposure) |
| • compliance obligations | (financial liabilities) |
| • stakeholder interest | (ethical obligations) |
| • operational considerations | (sensitivity to climatic change) |
| • future plans | (mergers and acquisitions) |

# How do you Evaluate Carbon Assets and Liabilities?

The International Financial Reporting Interpretations Committee (IFRIC) released IFRIC 3 'Emission Rights' on 2 December 2004.

IFRIC 3 interprets the accounting for companies participating in government greenhouse gas schemes.

- ASSET: account for the emission allowances they receive from governments as intangible assets, recorded initially at fair value.
- LIABILITY: requires companies, as they produce emissions, to recognize a liability for the obligation to deliver allowances to cover those emissions.

This interpretation was withdrawn June 2005 because government greenhouse gas schemes are in their infancy.

# How do you Evaluate Carbon Assets and Liabilities?

International Accounting Standards Board – April 11, 2007 – Announced a project to amend the existing accounting standards to better deal with the accounting issues around government greenhouse gas schemes.

Are allowances and credits (assets) in greenhouse gas schemes?

If so,

- how should a company account for any assets that it receives for less than fair value?
- how should assets be accounted for?
- how should changes in carbon assets and liabilities be reported in profit or loss?

# What is Carbon Risk?

Risk is a concept that denotes a potential negative impact to an asset or some characteristic of value that may arise from some present process or future event.

Carbon risk examines the potential negative impact climate change to the company's assets.

# What is Carbon Risk?

Carbon risk examines the potential negative impact climate change to the company's assets.

- climate change regulations (e.g., emission limits)
- indirect effect of incorporating climate change externalities on goods and services (e.g., increasing fuel costs)
- climatic change and its effect on operating conditions (e.g., water availability, temperature)
- availability of resources (e.g., feedstock, personnel)

# What Does Carbon Risk Have to do With Disclosure?

Disclosures in financial statements enables users to evaluate:

- the significance of financial instruments for the company's financial position and performance; and
- the nature and extent of risks arising from financial instruments, and how the company manages those risks.

# What is Carbon Risk Management?

It is not an Environmental Management System (e.g., ISO 14001). Why? Because EMSs are designed to deal with current risks and not future risks.

1. Understand your position (current emissions profile, requirements, capability to meet requirements, opportunities to develop assets)
2. Develop leading indicators to chart progress and evaluate business environment (data management systems, reporting structure)
3. Integrate climate change into business decisions (accounting, mergers & acquisitions, operations, expansions)
4. Have a climate change strategic plan

# What Should You be Disclosing about Climate Change?

1. Material carbon assets,
2. Material carbon liabilities,
3. Material climate change-related risks to your assets, and
4. If you have climate change risks, how you manage these risks.

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